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August 20, 1999

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

EX PARTE

Ms. Magalie Roman Salas
Office of the Secretary
Federal Communications Commission
445 Twelfth Street, SW
Washington, DC 20554

Re: CC Docket 94-1 (Price Cap Performance Review)
CC Docket 96-45 (Universal Service)
CC Docket 99-249 (Low-Volume Long Distance Users)
CC Docket 96-262 (Access Charge Reform)

Dear Ms. Salas:

On behalf of the Coalition for Affordable Local and Long Distance Service, and its members AT&T, Bell Atlantic, BellSouth Corporation, GTE, SBC and Sprint, I submit the attached Memorandum in Support of the Coalition for Affordable Local and Long Distance Service Plan, with three appendices. Included as Appendix A is a corrected copy of the proposal, which was previously filed with a letter by me dated July 29, 1999. In addition, as Appendix B, we are submitting preliminary draft proposed rules to implement the proposal. We are submitting the draft proposed rules in order to better assist the Commission and other interested parties in understanding the proposal.

Pursuant to section 1.1206 of the Commission's rules, two copies of this letter and the attached memorandum with appendices have been filed for each docket. Please contact me or Evan Grayer at Harris, Wiltshire & Grannis with any questions.

Sincerely,

John T. Nakahata KSM

John T. Nakahata

Counsel to the Coalition for Affordable Local and Long Distance Service

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Enclosures

cc: The Honorable William E. Kennard
The Honorable Susan Ness
The Honorable Harold W. Furchtgott-Roth
The Honorable Michael K. Powell
The Honorable Gloria Tristani
Larry Strickling, Chief Common Carrier Bureau
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Chris Wright, General Counsel

ORIGINAL

BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C.

In the Matter of	)	
	)	
PRICE CAP PERFORMANCE REVIEW FOR LOCAL EXCHANGE CARRIERS	))	CC Docket No. 94-1
	)	
FEDERAL STATE JOINT BOARD ON UNIVERSAL SERVICE	))	CC Docket No. 96-45
	)	
LOW-VOLUME LONG DISTANCE USERS	)	CC Docket No. 99-249
	)	
ACCESS CHARGE REFORM	)	CC Docket No. 96-262

MEMORANDUM IN SUPPORT OF THE COALITION FOR AFFORDABLE LOCAL AND LONG DISTANCE SERVICE PLAN

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ATTORNEYS FOR THE COALITION FOR AFFORDABLE LOCAL AND LONG DISTANCE SERVICE (CALLS)

SUMMARY

The Coalition for Affordable Local and Long Distance Service ("CALLS"), comprised of AT&T, Bell Atlantic, BellSouth, GTE, SBC, and Sprint, submits this explanatory memorandum of its proposed plan for interstate access charge and universal service reform. After debating these issues for close to 20 years, the members of the Coalition have come together to propose a plan for the next five years that will promote comparable and affordable universal service, lower long distance bills, and promote competition in rural and residential markets. Today's universal service system, which relies on implicit support from interstate access charges, is inconsistent both with the development of competition in these markets and with the advent of new technologies such as packet switched networks. The end result of this plan will be to promote job creation and economic growth.

The plan has three main, interdependent pillars. First, it establishes a portable universal service fund that will provide explicit support to replace support currently implicit in interstate access charges. Second, the plan simplifies the patchwork of current common line charges into one subscriber line charge ("SLC"), and provides for deaveraging of those charges in a manner that will not undermine comparable and affordable universal service. Third, the plan establishes a "social compact" under which traffic-sensitive switched access rates will fall significantly and then be frozen, on average, at rates that are 50 percent lower than prevail today.

CALLS believes the public interest would benefit significantly if the Commission seized this opportunity to reform today's unsustainable system by adopting the plan before its implementation date of January 2000. These reforms will benefit consumers, and bring the Commission a giant step closer to implementing Congress' vision when it passed the Telecommunications Act of 1996.

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Washington, D.C.

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MEMORANDUM IN SUPPORT OF
THE COALITION FOR AFFORDABLE LOCAL AND LONG DISTANCE SERVICE PLAN

I. INTRODUCTION

The members of the Coalition for Affordable Local and Long Distance Service ("CALLS" or "Coalition"), which includes AT&T, Bell Atlantic, BellSouth, GTE, SBC, and Sprint, by letter to the Chairman and Commissioners dated July 29, 1999,[1] submitted an integrated universal service and interstate access reform plan covering price cap incumbent local exchange carriers ("ILECs"). The plan is designed to be implemented in January 2000 and would apply to those carriers electing to participate.[2] All signatory price cap LECs commit to participate if the Commission adopts the plan as submitted. Also attached hereto are preliminary draft proposed rules to implement the plan with respect to the signatory price cap LECs.[3]

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1 Letter from John T. Nakahata, Counsel to CALLS, to Magalie Roman Salas, CC Docket Nos. 96-45, 96-262, 94-1, and 99-249 (filed July 29, 1999). A copy of the proposal, with technical corrections, is attached as Appendix A.

2 The specific implementation date may need to accommodate Y2K implementation, but this need not create a substantial delay.

3 *See,* Appendix B.

Consumers benefit significantly from this plan. First, the plan calls for per minute interstate access charge rates to be slashed in half. These reductions will lead to lower long distance bills. Cutting per minute access prices will also spur innovation and the development of new pricing packages for telecommunications services. Second, through a combination of universal service support and caps on flat-rated charges, rural and urban rates stay within a "fair range" of one another, thereby protecting rural consumers from unaffordable rates. Third, the plan will spur the development of competition in residential and rural markets by creating portable universal service support and allowing for limited deaveraging of rates. Fourth, low income "Lifeline" consumers will see common line charges falling and lower long distance bills. Fifth, urban consumers benefit because the deaveraging provisions of the plan will facilitate lower rates in more populated areas. Finally, consumer bills will be simplified as confusing fees and charges are consolidated.

A. Overview of the Plan

The CALLS plan has three main, interdependent pillars.

First, it establishes an explicit interstate universal service fund that will provide support to replace $650 million of implicit support currently collected through interstate access charges. This support will be portable to competing LECs. It will also be sustainable as new technologies, such as packet-switching, allow more users to avoid paying long distance rates that reflect the implicit support embedded in per minute access charges.[4] The support will ensure that

[4] This universal service support mechanism makes explicit support that currently is implicit in interstate access charges of price cap companies. This mechanism is separate and distinct from the new federal high cost mechanism the Commission currently is developing that will provide federal support for intrastate rates of non-rural carriers. The Commission is in the process of identifying the amount and type of support that is implicit in interstate access charges of price cap companies, and recently sought comment on how interstate access charges should be adjusted once this support has been made explicit. Except with respect to

rural Americans continue to enjoy affordable telecommunications service, and will facilitate the development of competitive choices — both packet-switched and circuit-switched — in rural and urban markets.

Second, the plan simplifies the patchwork of current common line charges into one subscriber line charge ("SLC"), and provides for deaveraging of those rates without undermining universal service. These changes rationalize and simplify the existing pricing regime for interstate exchange access service, and will promote increased local competition in residential and rural markets.

Third, the plan establishes a "social compact" under which traffic-sensitive switched access rates will fall by approximately 50 percent and will then be frozen, on average, at these low levels. The target rate caps are the result of arm's length negotiations between interexchange carrier ("IXC") and ILEC members of the Coalition. In addition, the plan narrows the discrepancy between the interstate access rate structure and the current interstate access charge "exemption" used by Internet Service Providers ("ISPs"). By substantially lowering the traffic-sensitive costs of access, the plan lessens the opportunity for arbitrage and uneconomic bypass that currently threatens universal service.

Congress recognized in the Telecommunication Act of 1996 ("the 1996 Act") that universal service reform is a critical component of its "pro-competitive, deregulatory national

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Continued . . .

explicit support to replace implicit support in interstate access charges of signatory rural price-cap companies, this mechanism is also separate and distinct from any new support for rural carriers, upon which the FCC has not yet acted. *See*, Federal-State Joint Board on Universal Service, CC Docket No. 96-45, and Access Charge Reform, CC Docket No. 96-262. *See, Seventh Report and Order and Thirteenth Order on Reconsideration*, CC Docket No. 96-45 (*"USF Seventh R&O"), Fourth Report and Order*, CC Docket No. 96-262, and *Further Notice of Proposed Rulemaking* (*"High Cost Methodology Further Notice"*), FCC 99-119, at ¶¶ 123-35 (rel. May 28, 1999).

policy framework."[5] The Commission did likewise when it first implemented the 1996 Act, characterizing its interstate *Access Charge Reform Order*[6] and *Universal Service Order*[7] as two parts of its "competition trilogy." Notwithstanding widespread recognition of the need for reform, restitching the "patchwork quilt of implicit and explicit subsidies"[8] that had supported universal service before the 1996 Act continues to be a difficult task. In those two critical orders, the Commission outlined, but did not complete, solutions that would identify implicit universal service support embedded in interstate access charges and move that support into competitively-neutral, non-discriminatory, and explicit universal service mechanisms. Today, three and a half years after enactment of the 1996 Act, those two critical parts of the "competition trilogy" await completion.

Events since 1996 — and May 1997 when the Commission released its original *Access Charge Reform* and *Universal Service Orders* — make it even more imperative that universal service and interstate access charge reform be completed and implemented. In 1997, the Commission identified three basic forms of implicit support for universal service:

(1) geographic rate averaging between higher cost and low cost areas;

(2) support for residential service through higher charges on business lines; and

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5 H.R. Rep. No. 104-458, at 1 (1996).

6 Access Charge Reform, *First Report and Order*, 12 FCC Rcd 15982, 15985 (1997) ("*Access Charge Reform Order*").

7 Federal-State Joint Board on Universal Service, Report and Order, 12 FCC Rcd 8776, 8781 (1997) ("Universal Service Order"), aff'd in part, rev'd in part, and remanded sub nom. Texas Office of Pub. Util. Counsel v. FCC, No. 97-60421, 1999 U.S. App. LEXIS 17941 (5th Cir. July 30, 1999).

8 Implementation of the Local Competition Provisions of the Telecommunications Act of 1996; Interconnection between Local Exchange Providers and Commercial Mobile Radio Service Providers, *First Report and Order*, 11 FCC Rcd 15499, at ¶ 5 (1996).

(3) higher, above-cost usage charges to support costs of serving low usage subscribers.[9]

All three of these implicit mechanisms are present today in interstate access charges. The Commission, in 1997, correctly recognized that "this system is not sustainable in its current form in a competitive environment."[10] Moreover, the Commission predicted that "this incentive to entry by competitors in the lowest cost, highest profit market segments (caused by raising some rates significantly above cost) means that today's pillars of implicit subsidies — high access charges, high prices for business services, and the averaging of rates over broad geographic areas — will be under attack."[11] The Commission therefore stated at that time that it would retain its current system only until January 1, 1999.

Today, the transition to explicit universal service support and sustainable, pro-competitive access rate structures remains incomplete, while the Commission continues to seek ideal solutions to these complex and critical issues. As the Commission predicted, however, the market-opening reforms created by the 1996 Act have led to the development of growing business market competition, particularly in urban areas. Universal service and interstate access charge reform can no longer wait. If reform is further delayed, solutions that preserve universal service will only become more difficult and more abrupt. The regulatory uncertainty that has characterized telecommunications markets since the 1996 Act will continue to "overhang" all investment decisions, chilling investment and delaying the expansion of competition into residential and rural markets.

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9 See, Universal Service Order, at ¶ 11; see also, USF Seventh R&O, at ¶ 6.

10 Universal Service Order, at ¶ 17.

11 Id.

Moreover, implicit support today is increasingly threatened by technological and competitive changes. For instance, packet-switched network services such as cable modems and xDSL services are continuing to develop at an accelerating rate. As these networks develop and become increasingly capable of providing alternative means of transmitting voice services, particularly long distance services,[12] it will become easier for end users to avoid supporting universal service through implicit universal service support mechanisms embedded in interstate access charges. Unless the present "patchwork quilt" of support can be replaced with universal service support mechanisms sewn from a single, cohesive cloth, the system of universal service support and emerging packet networks will be on an unnecessary collision course.[13] To maintain both the "unregulation" of the Internet and universal service requires changing existing universal service and interstate access charge mechanisms.[14]

As the Commission has also recognized, implicit support is not just unsustainable, but it actually impedes the development of choice and competition in residential and rural markets. As the Commission recently observed, "implicit support can also delay or deny the benefits of competition to residential and high-cost consumers if a competitor finds that it is unable to compete against an incumbent's artificially low rates."[15] By contrast, "explicit mechanisms may encourage competitors to expand service beyond urban areas and business centers into all areas

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[12] *See*, Communications Daily, at 9 (July 22, 1999); "*Covad Announces First Alliance to Deliver Voice Over DSL Services to Small Business*," Covad Press Release, at www.covad.com (July 21, 1999); Seth Schiesel, "*Hello Operator? Get me the Internet*," N.Y. Times (March 24, 1999).

[13] To address universal service issues fully could require a combination of state and federal action. *See* note 4, *infra*.

[14] *See generally*, Jason Oxman, *The FCC and the Unregulation of the Internet,* OPP Working Paper No. 31 (Office of Plans and Policy rel. July 19, 1999).

[15] USF Seventh R&O, at ¶ 7.

of the country and to all Americans, as envisioned by the 1996 Act."[16] As the Commission correctly noted, "[e]fficient competition in local markets is most likely to occur when rates for services, after factoring in explicit universal service contributions or support, reflect the underlying cost of providing service."[17]

The CALLS plan addresses today's unsustainable and, in residential and high-cost areas, competition-unfriendly system by directly tackling all three sources of implicit universal service support in interstate access charges. It does so through a combination of $650 million of explicit universal service support targeted to those areas that are the highest cost to serve, continued reform of the common line rate structure to increase economic efficiency and competitive neutrality, and targeted reductions of switched access charges.

Universal service and interstate access charge rate structure reform alone will not, however, create the regulatory certainty necessary to facilitate the development of competition, nor would it maximize consumer welfare. It is also not possible, from a practical perspective, fully to resolve universal service support issues without also addressing the level and the structure of interstate access rates. The third pillar of the CALLS plan, therefore, revises and simplifies the Commission's system of price cap rate regulation. This simplification cuts per minute access charges dramatically, and stabilizes a price cap system that has been in almost-continual flux since it was adopted. Rather than the complex rules that have led to three price cap plans in eight years, consumers and industry participants will benefit from a simplified system where average switched access for a telephone tariff filing entity will be capped at low per minute rates.

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16 *Id.* at ¶ 9.

17 *Id.* at ¶ 8.

The CALLS plan benefits consumers, fundamentally preserves and enhances universal service, and creates an interstate access charge rate structure that will be more consistent with technological developments. Adoption of this plan will result in a "cease-fire" for at least a critical five year period as telecommunications markets accelerate the transition to greater and more widespread competition. The CALLS plan, taken as a whole and only as a whole,[18] accomplishes all these goals in a manner consistent with sound economic principles, paving the way for the marketplace to deliver on the twin promises of the 1996 Act — broad growth of competition and affordable universal service in all telecommunications markets.

B. Summary of CALLS Plan

The full text of the CALLS plan is set forth in Appendix A. In summary, the plan incorporates the following elements into an integrated universal service and interstate access reform package:

1. ***Common Line Reform***

    a) As required by the Fifth Circuit,[19] local telephone companies recover universal service contributions explicitly from end users, not through carrier-paid interstate access charges.

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[18] Although the members of CALLS have all made hard concessions in reaching agreement on these reforms, each has recognized the predominant importance of a rational and integrated plan for the future. The CALLS plan as developed, therefore, represents a delicate balancing of competing policies that the members of CALLS urge the Commission not to disturb. Specifically, while all members support and endorse the plan as presented to the Commission, any changes may cause some or all members to withdraw their support.

[19] *Texas Office of Pub. Util. Counsel*, 1999 U.S. App. Lexis 17941, at 64-66.

b) Residential SLCs for price cap carriers are capped at $5.50 initially, with caps gradually increasing to $7.00 by July 2003. Deaveraged, multiline business SLCs are capped at $9.20 per month. $650 million in universal service funding explicitly and transparently supports these caps without creating additional implicit support.

c) All residential PICC-related charges — flat-rate charges from local companies to long distance companies that are today billed by long distance companies to subscribers — are folded into SLCs. Residential consumers will not see a federal common line charge on their bill other than the SLC. The transition of common line rates away from above cost per minute (carrier common line) and multiline business PICC charges continues, and, after the CCLC and multiline business PICC are eliminated, companies will be permitted geographically to deaverage SLCs as they geographically deaverage rates for unbundled loops.

2. ***Universal Service***

a) $650 million per year in explicit universal service support replaces $650 million of implicit support in interstate access charges. This universal service support is portable to all competing LECs, and targeted to high cost areas.

b) Lifeline support is increased to protect low-income consumers from all effects of these changes, including the consolidation of

PICCs with SLCs. This consolidation eliminates PICC-related charges for Lifeline customers with no offsetting increases in fixed monthly service rates.

3. ***Switched Access***

a) Per minute interstate access charges are cut in half, from an average of over 1.1 cents per access minute to just over 0.55 cents per access minute, dropping significantly faster than they would under the Commission's existing rules. These reductions are accomplished by continuing an X-factor of 6.5% and targeting "X-factor" adjustments to switched access elements until switched access charges other than carrier common line charges reach 0.55 cents per minute for the Bell Companies and GTE, and 0.65 cents per minute for other price cap incumbent LECs. Thereafter, average switched access rates for a filing entity are capped at these levels until at least January 1, 2005. Per minute access charge reductions will result in lower long distance bills.

Set forth below are further, more detailed descriptions of each of the "three pillars" of the CALLS plan.

II. A SUSTAINABLE, PRO-COMPETITION, AFFORDABLE, AND SIMPLIFIED COMMON LINE RATE STRUCTURE

A. Common Line Rate Elements are Simplified and Sustained by Explicit Universal Service Support

As the Commission has recognized in its Access Charge Reform orders, reform of common line pricing is a critical step in meeting section 254's command to establish mechanisms to preserve universal service and to create such explicit support as is necessary to provide sufficient support.[20] The CALLS plan would permit the Commission to continue, and simultaneously to simplify, this reform process. Consistent with this mandate of the 1996 Act, these reforms will encourage more competitive entry into local markets, and preserve and enhance universal service by substituting explicit support for existing implicit support inherent in geographically-averaged rates and inefficient rate structures.

To accomplish these important goals, the plan would immediately eliminate all residential and single-line business PICCs, and reduce the multiline business PICC to no more than $4.00 per month.[21] The primary residential SLC cap (but not necessarily the rate charged to customers) becomes $5.50, effective January 2000, increasing over three years to $7.00.[22] Similarly, the non-primary residential SLC cap (but not necessarily the rate charged to customers) increases to $7.00 in January 2000, with no further increases.[23] As with the Commission's existing SLC caps, the actual rate in most cases will be less. Ultimately, primary and non-primary residential line rates are unified, and distinguishing between these lines is no longer required. Toll rates can thus decrease as this implicit support from per minute access charges is eliminated. Multiline business SLCs remain capped at $9.20, although as is the case today, actual rates will be in most cases, substantially below the cap.[24]

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[20] *E.g.*, *Access Charge Reform Order*, at ¶ 75. Section 254(e) directs that universal service support "should be explicit." 47 U.S.C. § 254(e); *see also*, *USF Seventh R&O*, at ¶¶ 8, 43.

[21] Appendix A at 2.1.2.1, 2.1.3.1, and 2.1.4.1.

[22] *Id.* at 2.1.2.2.1 and 2.1.2.2.2.1.

[23] *Id.* at 2.1.3.2.1 and 2.1.3.2.2.1.

[24] *Id.* at 2.1.4.2.1 and 2.1.4.2.2.1.

All SLC caps are sustained through explicit universal service support, as discussed in Section III, *infra*. Accordingly, unlike today's system of SLC caps, this new system will not generally rely on implicit interstate access charge-based support. These caps are set at levels that will be affordable, and Lifeline support will be increased so that total service cost will be reduced for low-income consumers.

B. Reform of the Common Line Rate Structure is Necessary to Promote Competition and Preserve Universal Service.

1. *Controlled and capped increases in residential SLCs will promote competition.*

As the Commission and the Fifth Circuit have recognized, moving from implicit usage-based and business charge-based universal service support to explicit support is an essential step in the development of increased competition for all classes of customers.[25] Indeed, as the Commission has repeatedly observed, implicit universal service support through artificial regulatory pricing conventions is not sustainable in the face of competition.[26] There is widespread consensus among economists that when costs are fixed, as loop costs are, markets tend to push prices toward flat-rated, rather than usage-based, price structures.[27] The current rate structure does not do that. By inflating usage and business charges above market-based levels, it instead promotes competition for high-volume, typically high-revenue, low-cost business users.

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25 *USF Seventh R&O*, at ¶¶ 8, 43; *Texas Office of Pub. Util. Counsel*, 1999 U.S. App. Lexis 17941, at 64-66.

26 USF Seventh R&O, at ¶ 7.

27 Alfred E. Kahn and William B. Shew, Current Issues in Telecommunications Regulation: Pricing, 4 Yale J. on Reg. 191, 203-04 (1987); David L. Kasserman and John W. Mayo, Cross-Subsidies in Telecommunications: Roadblocks on the Road to More Intelligent Telephone Pricing, 11 Yale J. on Reg. 119, 125 (1994); Steve G. Parsons, The Economic Necessity of an Increased Subscriber Line Charge (SLC) in Telecommunications, 48 Admin. L. Rev. 227, 235-36 (1996).

The regulatory structure encourages new entrants to show considerably less interest in serving residential customers, in part because the current rate structure keeps incumbent LEC rates for these customers artificially low.[28]

The plan's SLC reforms represent a better way for the Commission to bring to the residential customer the increased innovation, improved service, and expanded choice the 1996 Act promised. SLCs that more closely reflect the common line costs of each individual line promote increased competition for all classes of customers, particularly residential and single-line business customers. Correspondingly, by eliminating the recovery of additional non-traffic sensitive common line costs through per minute or indirect charges, the plan increases the economic rationality of the common line rate structure. This increased economic efficiency and corresponding gains in consumer welfare will redound to the benefit of all Americans.

The plan's reforms also will relieve growing pressure on the Commission to regulate the Internet. For instance, packet-switched services, including Internet Protocol ("IP") services, increasingly will be able to provide substitutes for circuit-switched services. As these packet-switched services emerge, they will make usage-based per minute implicit universal service support unsustainable. Typically, providers of packet services charge on a flat-rated basis, rather than by the minute. In fact, flat-rated pricing is one of the potential efficiencies of a packet-based network, which early packet-based retail offerings such as cable modems and xDSL services reflect. A support system that relies on per minute access charges cannot, therefore, survive the emergence of packet services without imposing a time-metered rate structure on them — a pricing model the consumer market for IP services has already rejected. By significantly

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[28] Other approaches to common line reform, such as continued reliance on substantial carrier charges, whether flat or per minute, do not provide a reasonable mechanism for reducing

reducing the traffic-sensitive prices of switched access services, the CALLS plan substantially resolves these issues, reduces opportunities for arbitrage, and permits the development of rational pricing structures for all services.

The plan, by unifying SLCs, PICCs, and minute-based carrier common line charges into a single SLC, also facilitates competition by simplifying the common line rate structure. Line charges that are consolidated and paid by the end user customer selecting the service provider are more likely to be subject to head-to-head price competition than charges that are passed only indirectly to end users through averaged toll rates. Under this approach, residential and rural line charges will be structured to face competitive pressure.

Moreover, simplifying a bewildering rate structure is itself a consumer benefit. Thousands of calls and letters to carriers, Congress, and the Commission confirm that ratepayers are confused by these charges, particularly PICC-related charges, and do not understand their basis. As the Commission has recognized in its *Truth in Billing* proceeding, competition functions best when customers understand what they are paying for and can make informed comparisons among service providers.[29] By facilitating such comparisons, the plan's reforms will assist consumers as they choose among competing services and providers.[30]

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implicit support, consistent with Section 254(e). *See*, *Texas Office of Pub. Util. Counsel,* 1999 U.S. App. Lexis 17941, at 66.

29 *See generally,* Truth-in Billing and Billing Format, CC Docket No. 98-170, *First Report and Order and Further Notice of Proposed Rulemaking*, FCC 99-72 (rel. May 11, 1999).

30 The plan also eliminates the distinction between primary and non-primary lines over a three year period, ending another source of consumer confusion.

2. ***The new SLC caps will ensure that rate levels remain affordable.***

The CALLS plan establishes SLC caps for both primary residential and single line business lines that start at $5.50 and rise to a maximum of $7.00 monthly. Like current SLCs, this amount represents a cap. Most residential SLCs will never reach $7.00 per month.[31] These caps are supported by a $650 million explicit interstate safety net. The plan also expands Lifeline support to ensure that those most at risk from small increases remain connected to the network. Lifeline consumers — who are most vulnerable to rates becoming "unaffordable" — would pay no monthly SLCs, pay no PICC-related charges (which many pay today), and see lower long distance bills. This combined result will strengthen subscribership among low-income consumers.[32]

For non-Lifeline consumers, the $5.50 initial cap for the consolidated SLC will not affect affordability. Today, non-Lifeline residential end users who pre-subscribe to calling plans pay approximately $5.00 per month in combined SLC and IXC-billed PICC-related charges. Furthermore, the caps under existing rules on primary residential PICCs will increase by another $0.50 on July 1, 2000, making it likely that, even under current rules, most residential customers would pay combined SLC and IXC-billed PICC charges of approximately $5.50 as of July 1, 2000. Therefore, the initial fixed common line charges under the plan will be approximately the same as under current rules, subject only to a 6-month timing shift. There is no basis for

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[31] As of July 2003, we estimate that the average residential SLC across all price cap LECs will be $6.15.

[32] By eliminating residential PICCs and relying on low income support mechanisms to assist those for whom affordability is of greatest concern, this plan also will address many of the Commission's concerns raised in its recent Low Volume NOI. *See*, Low Volume Long Distance Users, CC Docket No. 99-249, *Notice of Inquiry*, FCC 99-168 (rel. July 20, 1999) (*e.g.*, Statement of Michael K. Powell, concurring, questioning the correlation between long distance calling patterns and income).

classifying the plan's $5.50 consolidated SLC as "unaffordable" for non-Lifeline customers on January 1, 2000, when the $5.50 combination of SLCs and PICCs that will result under existing rules is considered "affordable" on July 1 of the same year.[33]

In subsequent years, the plan increases the primary residential and single line business SLC cap to $7.00 in three phases. The primary residential and single line business SLC cap rises to $6.25 on January 1, 2001, to $6.75 on July 1, 2002, and to $7.00 on July 1, 2003.[34] There is no empirical evidence that these new common line rate structures will cause subscribers to drop off the network. In fact, the historical evidence suggests that subscribership will improve. Past experience shows that the shift away from per minute access charges to flat charges has had an overall positive effect on telephone subscribership. In 1984, when the first SLCs were adopted, telephone subscribership was 91.8 percent. Due in part to the creation of the SLC and later the PICC, usage sensitive interstate access rates — and, in turn, long distance rates — have fallen, and subscribership has increased. By 1989, when residential SLCs first reached $3.50, telephone subscribership had risen to 93.3 percent. Today, with SLC and PICC-related charges totaling approximately $5.00 per month, and with additional charges for the Telecommunications Relay Service ("TRS") and number portability, telephone subscribership is over 94 percent.[35]

Moreover, as a series of studies has indicated, overall toll charges have a more substantial impact on whether telephone service is affordable than do fixed monthly charges.[36] By

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33 Furthermore, the initial proposed SLC cap of $5.50 is the equivalent, in inflation adjusted terms, of a $3.50 SLC in 1984 dollars, the year the SLC was instituted.

34 *See*, note 22, *supra*.

35 Alexander Belinfante, *Telephone Subscribership in the United States*, (Com. Car. Bur., Ind. Anal. Div. rel. May 1999), at Table 1; *see also*, *USF Seventh Report and Order*, at ¶ 38.

36 Chesapeake and Potomac Telephone Company's Submission of Telephone Penetration Studies, Formal Case No. 850 (filed October 4, 1993); Field Research Corporation, *Affordability of Telephone Service — A Survey of Customers and Noncustomers*, 1993

dramatically reducing switched access charges, which can thus lower long distance bills, it is likely that the plan would, in fact, make telephone service more affordable. Based on all of this experience, with full protection for Lifeline customers, and with further dramatic reductions in switched access charges as an integral part of this plan, there is no reason to believe that the gradual transition of caps on flat-rated charges from \$5.50 to \$7.00 over the next four years will undermine subscribership.

Indeed, the marketplace has now provided factual evidence to satisfy the Commission's concern that caused it to create PICCs in 1997 rather than simply raise SLC caps. At that time, the Commission stated that it was concerned that SLC increases could affect affordability.[37] Since they were implemented in 1998, however, the PICCs have been passed on to end users at even higher unit rates than the Commission had contemplated, without leading to lower subscribership levels. Moreover, the CALLS plan secures affordability by setting an ultimate cap of \$7.00 for residential and single-line business customers in the most rural areas. Carriers will receive explicit universal service support to support these caps.[38]

The CALLS plan also narrows interstate regulatory distinctions between multiline business and other lines by substantially narrowing, and in many cases eliminating, the gap

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Continued . . .

(study funded by GTE-California and Pacific Bell, mandated by the California Public Utilities Commission); Milton Mueller & Jorge R. Schement, *Universal Service from the Bottom Up: A Profile of Telecommunications Access in Camden, New Jersey*, 12 *Information Society* 3 (April 1996); John Horrigan & Lodis Rhodes, *The Evolution of Universal Service in Texas* (September 1995) (working paper, LBJ School of Public Affairs). *See also,* Milton Mueller, Jr., *Universal Service* at 172 (1997).

37 Access Charge Reform Order, at ¶ 73.

38 Non-primary residential SLCs also will remain reasonable. Currently, non-primary residential lines are charged a SLC capped at \$6.07 and, where the end user does not pre-subscribe his or her second line, an additional PICC capped at \$2.53. Under the plan, non-primary lines will be subject only to the residential SLC of \$7.00.

between the multiline business SLCs and other SLCs. The plan retains the current $9.20 multiline business SLC cap, and it lowers the multiline business PICC cap to $4.00. In combination with the changes to the residential and single-line business common line rate structure, these facets of the plan immediately reduce the implicit support currently running from multiline business to other lines, accelerating a process set in motion by the Commission in the 1997 *Access Charge Reform Order.* In addition, the plan facilitates and accelerates the elimination of the Transport Interconnection Charge ("TIC"), a Commission priority under both competitive and economic principles, and a necessary response to the D.C. Circuit's *CompTel* remand.[39]

The Commission's prior decisions establishing the SLC and PICC already have brought per minute toll charges to their lowest levels in history, spurring demand for these services, making telecommunications services more affordable, and benefiting users of the interstate telecommunications network. The plan's additional simplified flat-rated recovery of common line costs, together with other changes in the plan, will pave the way for further innovation in long distance pricing, potentially enabling long distance providers to offer rate plans that resemble Internet flat-rates and wireless blocks of minutes.

3. ***SLC deaveraging will benefit consumers and preserve universal service.***

In addition to dramatically reducing implicit support by multiline business customers of the residential and single-line business rates,[40] the CALLS plan also substantially reduces the implicit support of rural rates by urban ratepayers through geographically averaged SLC charges. However, by integrating SLC deaveraging with explicit universal service support and deaveraged

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[39] Competitive Telecommunications Ass'n v. FCC, 87 F.3d 522, 536 (D.C. Cir. 1996).

[40] In most areas, the CCL and multiline business PICC will be eliminated entirely.

UNE loop rates, the plan strengthens both rural and urban competition, and ensures affordable rural rates. This action is another critical step in the development of increased competition and the preservation of universal service

This plan's approach to geographic deaveraging allows prices partially to reflect actual variations in the costs of providing service in varying geographic areas. Under the CALLS plan, deaveraging of SLCs may only be done after a state commission establishes deaveraged UNE rates by zone, and eliminates the CCL and PICC charges.[41] Deaveraged SLCs, thereafter, will reflect underlying variations in forward-looking loop and port costs within these zones. The plan protects high-cost customers by providing that no SLC, whether averaged or deaveraged, may exceed the overall SLC caps the plan establishes. Deaveraged SLCs may not generate more revenue than geographically averaged SLCs would have.

Although prices will begin to reflect geographic variations in the forward-looking cost of providing service, newly explicit universal service support will protect rural consumers against substantial rate increases and will support the capping of residential SLCs at $7.00 per month. Without these SLC reforms, the regulatory system will continue to provide undue incentives to carriers to compete primarily for business and the most high-volume residential subscribers. Preserving the status quo makes it less likely that rural and most residential consumers will see a real choice of telecommunications providers. This incentive structure itself threatens to erode current implicit support systems. If it were to continue, current regulation would channel competition to urban business centers, and the ILECs would lose urban business customers that

41 A carrier need not eliminate CCL and PICC charges prior to deaveraging by voluntary reductions. Appendix A at 2.1.5.6.1.

they would otherwise retain. As a result, the ILECs' revenue stream from multiline business users that supports service to other subscribers would diminish.[42]

The plan has built-in safeguards with respect to geographic deaveraging. First, deaveraging is not permitted except where an ILEC has also established state-approved UNE zone prices.[43] This safeguard ensures that deaveraging of SLCs will be pro-competitive, and will not inadvertently hamper UNE-based entry or ILEC competitive response. Second, an ILEC may not reduce multiline business SLCs below residential SLC prices in a given UNE pricing zone.[44] This ensures that all consumers in low cost areas share the benefits of SLC deaveraging. Third, SLCs of a given customer class — such as multiline business — cannot have a lower price in a higher cost zone than in a lower cost zone.[45] Fourth, price cap permitted revenues from deaveraged SLCs cannot exceed the revenues that would be permitted under price cap regulation for averaged SLCs.[46] Fifth, except with respect to voluntary reductions, an ILEC may not deaverage prior to eliminating multiline business PICCs and CCL.[47] This ensures that deaveraging does not increase implicit support. Sixth, except with respect to voluntary reductions, the plan establishes a minimum charge within the lowest cost zone, which allows consumers outside the lowest cost zone to share the benefits of SLC deaveraging.[48]

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[42] See, USF Seventh R&O, at ¶ 7.

[43] Appendix A at 2.1.5.1.

[44] *Id.* at 2.1.5.3.

[45] *Id.* at 2.1.5.4.

[46] *Id.* at 2.1.5.5. *See,* note 86, *infra.*

[47] Appendix A at 2.1.5.6.1. A "voluntary reduction" is one in which the incumbent LEC reduces prices other than by offsetting those reductions against increases in other SLC charges or Interstate Access-related USF support. Appendix A at 2.1.5.6.3.

[48] Appendix A at 2.1.5.6.2. *See,* note 86, *infra.*